



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

June 18, 1998

S. 1301

Consumer Bankruptcy Reform Act of 1998

As reported by the Senate Committee on the Judiciary on June 4, 1998

SUMMARY

S. 1301 would make many changes and additions to the laws relating to bankruptcy, including establishing a system of means-testing for determining eligibility for obtaining relief under chapter 7 of the U.S. bankruptcy code. CBO estimates that implementing S. 1301 would cost \$293 million over the 1999-2003 period—\$277 million in discretionary spending, which would be subject to appropriation of the necessary funds, and \$16 million in mandatory spending. In addition, we estimate that the bill would increase receipts by \$1 million a year. Because the bill would affect direct spending and receipts, pay-as-you-go procedures would apply.

S. 1301 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would have no significant impact on the budgets of state, local, or tribal governments.

DESCRIPTION OF THE BILL'S MAJOR PROVISIONS

Title I of S. 1301 would establish a system of means-testing for determining eligibility for relief under chapter 7 of the U.S. bankruptcy code. Title II would provide various procedural protections to debtors. Title III would:

- require the Administrative Office of the United States Courts (AOUSC) to receive and maintain income tax returns for all chapter 7 and chapter 13 debtors;
- require the AOUSC to collect and publish certain statistics on bankruptcy cases;
- require that at least one out of every 500 bankruptcy cases under chapter 13 or chapter 7 be audited by an independent certified public accountant;

- require the Executive Office for the United States Trustees (U.S. Trustees) to establish a program to educate debtors on financial management; and
- authorize 18 new temporary judgeships and extend five existing judgeships in 19 federal districts.

Title IV would make various technical changes to bankruptcy laws.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The bill would affect direct spending because it would authorize additional bankruptcy judgeships, and the salaries and benefits of these judges are considered mandatory. Costs for other personnel and administrative expenses of the courts associated with additional judgeships would be subject to the availability of appropriated funds. Enacting the means-testing provisions in Title I would result in fewer debtors filing for chapter 7 bankruptcy protection and more debtors filing for chapter 13 protection. As a result, CBO estimates a net increase in revenues from bankruptcy filing fees each year.

As shown in the following table, CBO estimates that implementing S. 1301 would cost the courts, the AOUSC, and the U.S. Trustees \$43 million in 1999 and \$277 million over the 1999-2003 period, subject to appropriation of the necessary funds. In addition, we estimate that mandatory spending for the salaries and benefits of bankruptcy judges would increase by \$1 million in 1999 and \$16 million over the 1999-2003 period. Additional revenues from filing fees would total \$5 million over five years. The costs of this legislation fall within budget function 750 (administration of justice).

BASIS OF ESTIMATE

For purposes of this estimate, CBO assumes that S. 1301 will be enacted by October 1, 1998, and that all estimated authorization amounts will be appropriated for each fiscal year.

By Fiscal Year, in Millions of Dollars

	1999	2000	2001	2002	2003
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CHANGES IN SPENDING SUBJECT TO APPROPRIATION

Means-Testing Litigation (Sections 101-102)					
Estimated Authorization Level	1	1	1	a	a
Estimated Outlays	1	1	1	a	a
Maintain Income Tax Information (Section 301)					
Estimated Authorization Level	6	5	6	7	9
Estimated Outlays	5	5	6	7	9
Data Compilation/Publication (Section 306)					
Estimated Authorization Level	2	6	8	8	9
Estimated Outlays	2	5	8	8	9
Audit Procedures (Section 307)					
Estimated Authorization Level	0	2	4	5	6
Estimated Outlays	0	2	4	5	6
Debtor Financial Management Training (Section 321)					
Estimated Authorization Level	40	33	32	26	27
Estimated Outlays	32	34	32	27	27
Support Costs for Additional Judgeships (Section 322)					
Estimated Authorization Level	3	9	10	10	11
Estimated Outlays	3	8	10	10	10
Total Changes					
Estimated Authorization Level	52	56	61	56	62
Estimated Outlays	43	55	61	57	61

CHANGES IN DIRECT SPENDING

Additional Judgeships (Section 322)					
Estimated Budget Authority	1	3	4	4	4
Estimated Outlays	1	3	4	4	4

CHANGES IN REVENUES

Decrease in Chapter 7 Filing Fees and Increase in Chapter 13 Filing Fees					
Estimated Revenues, Title I	1	1	1	1	1

a. Less than \$500,000 a year.

Spending Subject to Appropriation

The estimated increases in discretionary spending would be required to fund the additional workload that would be imposed on the courts, the AOUSC, and the U.S. Trustees. Currently, the U.S. Trustees are funded through the bankruptcy-related fees collected by the courts. Without additional statutory authority, these fees cannot be increased to cover any additional expenditures that would result from enacting the bill. Because the legislation does not provide for such increases in fees, any additional costs would be subject to the availability of appropriated funds.

Means-Testing (Sections 101-102). The means-testing provision in S. 1301 would require a bankruptcy judge to consider two factors when deciding if a debtor's petition for a chapter 7 bankruptcy would be abusive and therefore require dismissal or conversion to a chapter 13 case. First, the court would consider whether the debtor could repay 20 percent of his or her general unsecured claims. Second, the court would consider if the debtor filed the case in “bad faith.” Also, creditors would be allowed to bring motions claiming abuse of the bankruptcy system, unless the debtor and the debtor's spouse have combined current monthly income less than or equal to the national median income for a family of the same size. In addition, a creditor would have to pay the debtor's attorney's fees and litigation costs if the motion to dismiss the case was denied and not substantially justified.

Under S. 1301, CBO estimates that the U.S. Trustees would be required to compile and review income data necessary for means-testing and to participate in any litigation that would result from issues concerning eligibility. CBO expects that any additional data collection requirements would not pose a significant burden on the U.S. Trustees and thus would require no additional appropriations. However, we expect that the U.S. Trustees would incur additional costs for the work that would result from increased litigation.

Based on information from the U.S. Trustees, CBO expects that the bill's means-testing provisions could increase litigation over a debtor's eligibility for chapter 7 relief because of potential conflicts between the courts and debtors over whether granting relief would be an “abuse” of the bankruptcy code. Under the bill, additional motions for dismissal would result as more objective criteria would be applied to a debtor's income and expenses and because creditors would have the ability to challenge petitions for chapter 7 relief. Some debtors whose petitions for chapter 7 relief would be denied under S. 1301 would undoubtedly appeal those decisions.

Although CBO cannot predict the amount of additional litigation, we expect that there would be some during the first few years following enactment of S. 1301, as parties test the new law's standards. We expect that the U.S. Trustees, who would become gatekeepers to the

bankruptcy system under the bill, would be heavily involved in any litigation that would result, at an estimated cost of about \$1 million annually through 2001. In subsequent years, the amount of litigation could diminish as precedents are established, and we estimate that costs would decrease to about less than \$500,000 annually.

Maintenance of Tax Returns (Section 301). This section would require the AOUSC to receive and retain tax returns for the three most recent years preceding the commencement of the bankruptcy case for all chapter 7 and chapter 13 debtors (about 7 million debtors over the 1999-2003 period). CBO estimates that appropriations of \$33 million over the next five years would be required to store and provide access to over 20 million tax returns.

Compilation and Publication of Bankruptcy Data and Statistics (Section 306). S. 1301 would require the AOUSC to collect data on chapter 7, chapter 11, and chapter 13 cases and to make the information available to the public. CBO estimates that appropriations of about \$33 million would be required over the 1999-2003 period to meet these requirements. Of the total estimated cost, about \$22 million would be required over the next five years for additional legal clerks, analysts, and data base support. The remainder of the estimated cost (\$11 million) would be incurred for compiling data and providing Internet access to records pertaining to bankruptcy cases.

Audit Procedures (Section 307). Beginning 18 months after enactment, S. 1301 would require that at least one out of every 500 bankruptcy cases under chapter 7 and chapter 13, plus other selected cases under those chapters, be audited by an independent certified public accountant. The U.S. Trustees estimates that about 1.2 million cases would be subject to audit in fiscal year 2000, increasing to about 1.8 million in fiscal year 2003. Assuming that about 0.25 percent of all cases would be audited and that each audit would cost about \$1,200 (in 1998 dollars), implementing this provision would require appropriations of \$2 million in fiscal year 2000 and \$17 million over the 1999-2003 period. Section 307 also would require the Attorney General to attempt to recover some of the costs of audits from debtors with sufficient income or assets. As a result, it is possible that net costs for this section could be less than the above estimate to the extent that debtors could contribute to the funding of the audits; however, CBO does not expect that such debtor contributions would be significant.

Instructional Courses in Financial Management (Section 321). This section would require the U.S. Trustees to establish a training program to educate debtors on financial management. Debtors would be required to undergo this training, or comparable training approved by the U.S. Trustees, as a condition of receiving relief from certain debts. Based on information from the U.S. Trustees, CBO estimates that about 1 million debtors would participate if such a program were administered by the U.S. Trustees in fiscal year 1999. In future years, CBO expects that private companies would offer comparable instruction that

could be taken by debtors (at their own expense) in place of a class administered by the U.S. Trustees. As a result, we expect that the number of debtors participating in the U.S. Trustees' instructional program would drop to about 600,000 by fiscal year 2002. At a projected cost of about \$40 per debtor, CBO estimates that the U.S. Trustees would require the appropriation of about \$158 million over the next five years to administer the training program.

Extension and Authorization of Bankruptcy Judgeships - Support Costs (Section 322).

This provision would extend five temporary bankruptcy judgeships and authorize 18 new temporary bankruptcy judgeships for 19 federal judicial districts. Based on information from the AOUSC, CBO assumes that one half of the 18 new positions would be filled by the middle of fiscal year 1999 and the other half would be filled by the start of fiscal year 2000. Also, we anticipate that all five temporary judgeships would be extended by fiscal year 2001. We expect that discretionary expenditures associated with each judgeship would average about \$400,000 (in 1998 dollars), after initial costs of about \$145,000. Therefore, CBO estimates that the administrative support of additional bankruptcy judges would require an appropriation of about \$3 million in 1999 and about \$43 million over the 1999-2003 period.

Direct Spending and Revenues

Means-Testing (Sections 101-103). CBO estimates that enacting the means-testing provisions would impose some additional workload on the courts. Although the U.S. Trustees would be responsible for conducting the initial review of financial information under either bill, CBO expects that the courts would also be involved in some level of review of such data. In addition, many bankruptcy judges expect that additional hearings and other court proceedings would be held over eligibility and income data.

Section 322 of this bill authorizes 18 new temporary bankruptcy judgeships and extends five existing temporary judgeships. Based on information from the AOUSC and other bankruptcy experts, CBO expects that such an increase in the number of bankruptcy judges would be sufficient to meet the increased workload. Assuming that the salary and benefits of a bankruptcy judge would average about \$152,000 a year (in 1998 dollars), CBO estimates that the mandatory costs associated with the salaries and benefits of these additional judgeships would be \$1 million in 1999 and about \$16 million over the 1999-2003 period.

The means-testing provisions would also affect the government's income from bankruptcy filing fees because they would cause changes in the number and type of bankruptcy filings. CBO projects that, as a result of this bill, about 5 percent of all chapter 7 debtors (about 48,000 out of 960,000 cases each year) would not file for any type of bankruptcy protection

and that about 5 percent of all chapter 7 cases would be filed as or converted to chapter 13 cases. With a reduction in chapter 7 filings, the government would lose income from chapter 7 filing fees. CBO estimates that for each case that would not be filed under chapter 7 or any other chapter, there would be a \$130 reduction in the filing fee paid to the government. Income from this fee appears in two different places in the budget. Of the \$130, \$70 is recorded as part of the offsetting collections to the U.S. Trustee System Fund and the Judiciary, and \$15 is recorded as governmental receipts (i.e., revenues). Under chapter 7, the remaining \$45 is paid to the private trustee assigned to the case and does not affect the federal budget. Assuming that fees for about 48,000 cases would no longer be collected each year, CBO estimates that enacting S. 1301 would result in a loss of about \$1 million a year in revenues and about \$3 million in offsetting collections. The loss of offsetting collections would reduce the amount available for spending by the U.S. Trustees and the AOUSC; however, CBO estimates that no additional appropriations would be required to replace this projected loss of fees because it would be matched by a reduction in workload associated with these chapter 7 cases.

The shift of cases from chapter 7 to chapter 13 would, in contrast, lead to greater fee collections. In contrast to the distribution of fees under chapter 7, \$60 of the \$130 filing fee is collected as a governmental receipt under chapter 13. (Private trustees are not paid out of the filing fee under chapter 13.) Thus, the government collects an additional \$45 for each shift of a case from chapter 7 to chapter 13. Because CBO expects that about 48,000 chapter 7 cases would be filed as or converted to chapter 13 cases, we estimate that revenues would increase by about \$2 million in each year. On balance, the net change in revenues would be an increase of about \$1 million each year.

PAY-AS-YOU-GO CONSIDERATIONS

Section 252 of the Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. As shown in the table below, CBO estimates that enacting S. 1301 would increase direct spending by about \$16 million over the next five years for the salaries and benefits of additional bankruptcy judges. In addition, enacting Title I would result in fewer chapter 7 debtors filing for bankruptcy protection and more debtors filing for chapter 13 protection. As a result, CBO estimates a net increase in revenues of about \$1 million each year. For purposes of enforcing pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

	By Fiscal Year, in Millions of Dollars										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Changes in outlays	0	1	3	4	4	4	4	4	3	2	2
Changes in receipts	0	1	1	1	1	1	1	1	1	1	1

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

S. 1301 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would have no significant impact on the budgets of state, local, or tribal governments. Federal bankruptcy statutes currently allow states to determine certain property exemptions for homes in bankruptcy cases. The bill would place some limits on the value of homes that individuals may protect under those statutes. While this provision may limit the application of some state laws, it may also free up additional resources in cases where a state or local government may have an outstanding tax claim.

PREVIOUS CBO ESTIMATES

On May 8, 1998, CBO transmitted a preliminary cost estimate comparing the means-testing provisions in S. 1301, as reported by the Senate Judiciary Committee's Subcommittee on Administrative Oversight and the Courts on April 2, 1998, with those in H.R. 3150, as introduced on February 3, 1998. The May 8 letter indicated that implementing the means-testing provisions in S. 1301 could require between 10 and 15 additional judges to meet the increased workload requirements that would be imposed on the federal court system under S. 1301. Costs for the salaries and benefits of judges, which are mandatory, would be about \$2 million annually. CBO further indicated that the means-testing provisions (in the subcommittee version of S. 1301) would not—by themselves—affect direct spending because the earlier version of the bill did not authorize any increase in the number of bankruptcy judges.

Subsequently, on June 5, 1998, CBO transmitted a cost estimate for H.R. 3150, as reported by the House Committee on the Judiciary on May 20, 1998. Unlike S. 1301, H.R. 3150 would not authorize additional bankruptcy judgeships. Thus, enacting H.R. 3150 would not affect direct spending. Differences in discretionary spending estimates between S. 1301 and H.R. 3150 reflect differences in the provisions of the two bills.

ESTIMATE PREPARED BY:

Federal Costs: Susanne S. Mehlman and Mark Grabowicz
Impact on State, Local, and Tribal Governments: Leo Lex

ESTIMATE APPROVED BY:

Robert A. Sunshine
Deputy Assistant Director for Budget Analysis